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SUBJECT: Sri Lanka Country Commercial Guide, FY 2004

REF: STATE 128494

1. Below is the Executive Summary of the Sri Lanka Country Commercial Guide, FY 2004. Per reftel, Post has sent the entire text of the Guide to Washington agencies, and will be uploading the guide to CS intranet soon.

BEGIN TEXT.

Country Commercial Guide

Sri Lanka

Fiscal Year 2004

EXECUTIVE SUMMARY

2. In 2003, Sri Lanka is expected to realize many political, economic and social rewards won through the cessation of armed conflict and the government's continuing peace initiatives. The year 2002 was a turning point for the country. After almost 20 years of armed conflict, the new government signed a ceasefire agreement with the Liberation Tigers of Tamil Eelam (LTTE). The initial agreement developed into an ongoing peace process supported by the Sri Lanka people and the international community. Eighteen months of peace has allowed positive economic growth and plans for reconstruction of the war-torn areas. Negotiations with the LTTE continue, though not always smoothly, into 2003. The outcome is uncertain, but the relative peace and stability brought by the cease-fire has created cautious optimism and increased activity by both the domestic population and the international business community.

3. The government has moved to capitalize on the peace by pushing reform and reconstruction at home and attracting assistance and investment from abroad. The commitment of \$4.5 billion at a June 2003 donor conference in Tokyo gives the government substantial resources to carry out its national objectives of rebuilding physical and social infrastructure and spurring economic growth. These objectives are identified in the Prime Minister's policy framework document, "Regaining Sri Lanka", which also includes the government's poverty reduction strategy. A portion of these funds (\$1.5 billion) will be spent to rebuild the areas most affected by the conflict - the north and east. Numerous projects have been identified for this financing, a combination of grants and concessional loans.

4. To implement reforms, and realize the goal of 8 percent annual growth, the government is focusing on progress in the peace process, and utilization of the increased flow of donor assistance in a quick and transparent manner. Earlier efforts to enhance private sector growth continue, including reforms in financial markets, labor, land, fiscal policy, telecom and privatization of state-owned enterprises. A new Information and Communication Technology initiative, eSri Lanka, aims to electronically connect and service the entire country. The labor force is being enhanced with education, skills training and a focus on productivity. Hoping to use trade to spur growth, Sri Lanka is emphasizing its central position in the region and key shipping lanes, Free Trade Agreements with its neighbors and its relatively friendly business climate to grow into a regional hub for manufacturing, commerce and transport.

5. The private sector also has responded to the peaceful environment with increased business activity and investment. Sri Lanka's economy expanded by 4 percent in 2002, and further progress was made on macroeconomic stabilization. Largely driven by services, GDP growth was 5.5 percent in

the first quarter of 2003, and this pace is expected to continue through the year. The SARS epidemic did not spread to Sri Lanka and tourism increased. On the negative side, in mid-May, southern Sri Lanka experienced extensive damage from severe flooding, though the impact on overall growth will be minimal. 16. The government has committed itself to reducing corruption; however, problems remain. Tender procedures are opaque, decision making is slow, enforcement of IPR rights is uneven, and bureaucracy, caused by a large public sector, hinders efficiency. Though the Prime Minister's party is strongly supported for its peace initiatives, tensions between the political parties of the Prime Minister and the President threaten domestic stability. Progress depends on the continuation of the peace process, policy adjustments, private sector development and structural reforms. Though still faced with substantial economic, social and political challenges, Sri Lanka accomplished much in 2002, a fact recognized by the international community. This external support, coupled with growing internal confidence creates the foundation for sustained growth and stability in 2003 and beyond.
END TEXT.

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